

TREASURY - GENERAL

STATE INVESTMENT COUNCIL

Common Stock and Issues Convertible into Common Stocks (Trust Funds)

Proposed Amendments: N.J.A.C. 17:16-42.1

Proposed Repeal: N.J.A.C. 17:16-42.4

Authorized By: State Investment Council, Peter A. Langerman, Director,
Division of Investment

Authority: N.J.S.A. 52:18A-91

Calendar Reference: See Summary below for explanation of exception to calendar requirement.

Proposal Number: PRN 2004-124

Submit comments by June 4, 2004 to:

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The agency proposal follows:

Summary

The proposed amendments to N.J.A.C. 17:16-42.1 and the repeal of N.J.A.C. 17-16-42.4 would eliminate the Approved Common and Preferred Stock and Convertible Securities List; permit the Division to invest in equities and securities that trade on an exchange in the United States or the over-the-counter market, with the exception of investments made for the Supplemental Annuity Collective Trust; and allow the Division to retain any distribution received as a result of a corporate action, even if the security does not meet the requirements of this subchapter

Given the thousands of individual investments comprising the Approved Lists, it has become unrealistic to expect that Council members will have extensive knowledge of

all of these investments. Eliminating the Approved Lists at N.J.A.C. 17:16-42.1 (b) and (c) and 41.4 (a), while at the same time providing criteria for selection of individual investments, gives recognition to the fact that the Council relies on the Division of Investment to have this in-depth knowledge and to select particular investments. Since the Division of Investment will be reporting to the Council on investment activities, the Council shall continue to be able to fulfill its role of monitoring of investments contained in the various portfolios.

Pursuant to the proposed amendments at N.J.A.C. 17:16-42.1 (c) the Division of Investment is authorized to purchase only investments that meet the requirements set forth in the subchapter. However, there may arise, from time to time, certain unique circumstances where the Division wishes to purchase an investment that does not meet the requirements set forth in the subchapter. In such event, the proposed amendments at N.J.A.C. 17:16-42.1 (c) provide that the Division could present justification to the Council, and the Council would have the authority to approve the purchase on a case-by-case basis.

Because the Division is providing a 60-day comment period on this notice of proposal, this notice is exempt from the rulemaking calendar requirement pursuant to N.J.A.C. 1:30-3.3(a)5.

Social Impact

There shall be no social impact from the proposed amendments and repeal, although the long term economic effects could benefit the State's taxpayers.

Economic Impact

The proposed amendments and repeal may provide an opportunity to earn greater returns as well as to broaden the diversification of the portfolios managed by the Division.

Federal Standards Statement

A Federal standards analysis is not required because the investment policy rules of the Division of Investment are under the auspices of the State Investment Council, and are not subject to any Federal requirements or standards.

Jobs Impact

The State Investment Council and the Division of Investment do not anticipate that any jobs will be generated or lost by virtue of the amendments and repeal.

Agriculture Industry Impact

The proposed amendments and repeal shall have no impact on the agriculture industry.

Regulatory Flexibility Statement

A regulatory flexibility analysis is not required, since the proposed amendments and repeal impose no requirements on small businesses as the term is defined in the Regulatory Flexibility Act, N.J.S.A. 52:14B-16 et seq., but regulate only the Director of the Division of Investment.

Smart Growth Impact

The proposed amendments and repeal are not anticipated to have an impact on the achievement of smart growth and implementation of the State Development and Redevelopment Plan.

Full text of the proposal follows (additions indicated in boldface **thus**; deletions indicated in brackets [thus]):

SUBCHAPTER 42. COMMON STOCKS AND ISSUES CONVERTIBLE INTO COMMON STOCKS (TRUST FUNDS)

17:16-42.1 Permissible investments

(a) The stock shall be issued by a company or bank incorporated or organized under the laws of the United States or any State thereof or of the District of Columbia, or by any international company that is included in the S&P 500 Composite Index[, except that the common stock and securities for the Supplemental Annuity Collective Trust Fund shall be listed on a securities exchange in the United States, as required by N.J.S.A. 52:18A-115].

[(b) The Director shall submit a list of common stocks and convertible securities to the Council for its approval. Such list may be amended or enlarged from time to time subject to the Council's approval and shall be designated the "Approved Common and Preferred Stock and Convertible Securities List."]

(b) The common stock and securities must trade on an exchange in the United States or over-the-counter market, except that the common stock and securities for the Supplemental Annuity Collective Trust Fund shall be listed on a securities exchange in the United States, as required by N.J.S.A. 52:18A-115.

[(c) The Director shall select for purchase issues of common stocks and convertible securities from the "Approved Common and Preferred Stock and Convertible Securities List."]

(c) Notwithstanding the restrictions contained in this subchapter, the Council may approve the purchase of common stocks on a case-by-case basis.

(d) Notwithstanding the above restrictions, the Director may:

1. (No change.)
2. Purchase the convertible issue of a company, the common stock of which qualifies for investment [and is on the "Approved Common and Preferred Stock and Convertible Securities List"] **under this subchapter**; [and]
3. Purchase up to one percent of any eligible fund's assets in new public offerings of companies without prior approval of the State Investment Council provided, however, approval will be sought at the next regularly scheduled Council meeting **in the event the security does not subsequently meet the requirements of this subchapter.** [In the event] **If** approval is not granted, the securities will be sold within three months of the Council's disapproval[.] ; **and**

4. Retain any distribution received as a result of a corporate action, even if the security does not meet the requirements of this subchapter.

17:16-42.4 [Approved Common Stock and Convertible Securities List] (**Reserved**)

[(a) The “Approved Common and Preferred Stock and Convertible Securities List” is a list of those companies whose stocks can be purchased by the eligible funds. Additions to or deletions from the List shall be made by the Council, in its discretion, based, respectively, upon the presence or absence of the following:

1. The company shall have growth in revenues and earnings which exceed growth in the Gross Domestic Product;
2. The company shall have a strong market franchise, unique products and proven marketing capability;
3. The company’s management shall have demonstrated the ability to preserve profit margins, to avoid earnings surprises and to take the needed initiatives to preserve and improve upon the company’s strengths;
4. The company shall have capitalization which is not heavily leveraged, thereby allowing it more flexibility to finance future expansion;
5. The company shall not be unduly capital intensive, which might expose it to the necessities of raising capital at times when capital markets are unduly expensive;
6. The company shall demonstrate that it can generate capital internally for growth;
7. The market for the company’s shares shall have enough liquidity to permit the orderly acquisition and disposition of a full position; and
8. The company shall have conservative accounting practices.

(b) Companies which are not in conformance with (a) 1 through 8 above may be added to or retained on the List, on a case-by-case basis, if the Council determines that the company is otherwise financially secure and presents a sound investment opportunity.]